



MONTANA LEGISLATIVE BRANCH

Legislative Fiscal Division

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Legislative Fiscal Analyst
CLAYTON SCHENCK

DATE: March 1, 2006

TO: Legislative Finance Committee

FROM: Alan Peura, Fiscal Analyst

RE: Postsecondary Education Policy and Budget Subcommittee

The Postsecondary Education Policy and Budget Subcommittee (PEPB) is working on the following six projects during the 2005-2006 interim:

Project #1 – Policy Goals/Accountability Measures for Montana University System (MUS):

Under this project, PEPB has forged a set of Shared Policy Goals and Accountability Measures that has been agreed to by the subcommittee as well as the Montana Board of Regents (see attached signed document).

This document is to serve as the foundation for PEPB to clarify to the university system what policy goals that the legislature is interested in as part of the 2009 biennium budget. And from this policy foundation, PEPB is considering a series of funding initiatives put forth by the Commissioner of Higher Education, to potentially recommend New Proposal-DP's for funding in the next budget, together with building in accountability measures (see staff report from December attached) as part of HB2 (see MUS funding initiatives list attached).

A work group from the PEPB has been formed to consider these initiatives in greater depth, including attending the Board of Regents meeting in Dillon (March 1-3) to participate in the Regents budget subcommittee discussions.

Project #2 – Review Current Funding Formulas and Consider Alternative Models

Under this project, PEPB conducted a review of other state funding models to determine whether there are best practice options or other policy considerations for state funding formulas to support the university educational units (campuses).

The attached staff report was discussed at the PEPB meeting on February 23, 2006 and the subcommittee has asked staff to complete additional research on some of these budget models for further consideration at the June meeting.

Project #3 – Shared Leadership Initiatives

This project has the PEPB monitoring the \$5 million-plus appropriation in the 2007 biennium to the university system to support the three initiatives related to the shared leadership for a stronger Montana economy project. The Commissioner of Higher Education submitted the attached summary report at the February 23, 2006 meeting, but due to time constraints the report was not discussed in depth. There will likely be a follow-up report at a subsequent meeting, in order to allow PEPB members to evaluate the outcomes of these initiatives and the impact of the state funding.

Project #4 – Governor's Scholarship Program

In the current biennium, the legislature approved the new Governor's Scholarship Program, appropriating \$1.5 million to support need-based and merit-based scholarships for Montana resident students. The subcommittee has received an early report from the Commissioner of Higher Education on the status of first year of this program (see attached report). At the August PEPB meeting there will be an update report that will specifically address PEPB interests in student retention rates and continuing progress in the 2-year and 4-year scholarships.

Project #5 – Regents Allocation Model Redesign

The Board of Regents is conducting a redesign of the calculation model and formula that is used to disburse the state appropriation across the campuses of the MUS.

There has been insufficient progress on this process to date to merit a report to PEPB, so there will be an in depth report to PEPB at the June meeting.

Project #6 – Monitor the 2009 Biennium Executive Budget

The Office of Budget and Program Planning has been invited to the June meeting to present their preliminary budget for the MUS to the PEPB.

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Joint Committee On Postsecondary Education Policy and Budget

59TH Montana Legislature

Room 110 Capitol Building * P.O. Box 201711 * Helena, MT 59620-1711 * (406) 444-2986 * FAX (406) 444-3036

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Shared Policy Goals and Accountability Measures for the Montana University System 2007 Biennium

This shared policy goals and accountability measures document represents a merging of the following four efforts that have involved leaders from the legislature, the executive and the university system over the past several years:

- 1) Board of Regents strategic goals and objectives
- 2) PEPB performance indicators and policy goals
- 3) The Shared Leadership for a Stronger Montana Economy initiatives
- 4) The University System campus quality measures

The documentation for these four efforts is incorporated by reference into this document in order to provide important background, history and context for these shared policy goals and accountability measures, in particular the shared commitments to quality, to accessibility, to affordability, to workforce development, and to an efficient, effective postsecondary education system.

It is the intention of the PEPB to review and approve this shared document and renew the biennial agreement with the Montana Board of Regents so that this document may become the basis of state public policy in regard to the Montana University System.

As a statement of public policy goals for higher education in Montana, it is important that this document reflects that PEPB is committed to academic quality throughout the Montana University System such that funding a high quality postsecondary education is a critical goal of the State of Montana. It is intended that this document will provide the policy direction from which a quality postsecondary education system in Montana will be maintained.

It is the intent that PEPB will then use this document to move forward with budget initiatives for the 2009 biennium budget, and other policy recommendations during the 2007 biennium interim and into the 2007 legislative session.

Please note: parenthesis after each performance measure lists the effort from which it was principally derived. E.g. "(2)" means the measure was derived principally from the PEPB Indicators from the last biennium. Some performance measures are a combination of more than one effort.

Shared Goal I:

Increase the overall educational attainment of Montanans through increased participation, retention and completion rates in the Montana University System (MUS).

- Prepare students for success in life through quality higher education, as measured by
 - Postsecondary education participation rates, with particular attention to Montana residents attending MUS institutions (4)
 - Completion rates (2)
 - Retention rates (2).
- Make higher education more affordable by offering more need-based financial aid grants and scholarships, as measured by
 - Reducing the gap between EFC (Expected Family Contribution) and average cost of attendance (1)
 - Percentage of students who receive financial aid or scholarships (1)
 - Average aid/scholarship award amount (4).
- Promote postsecondary education affordability, as measured by
 - Amount of state support as a percent of total personal income relative to peer states and historical levels (2)
 - Tuition as a percentage of median household income.
- Work collaboratively with the K-12 education system to increase high school academic preparedness, completion, and concurrent enrollment programs, as measured by
 - Increased dual enrollment and advanced placement programs (1,2)
 - Expanded outreach to students as to the importance and accessibility of postsecondary education and the quality of the Montana University System, including:
 - Expanded outreach to at-risk and disadvantaged students (1)
 - Expanded outreach to top academic achievers graduating from Montana high schools
 - Increased high school graduation rates (1,2,4).
- Increase postsecondary enrollment of traditional and non-traditional students through expanded outreach programs, evening/weekend programs, and 2-year programs (1).
- Improve distance and online learning by coordinating online delivery of education across the entire Montana University System (3).

Shared Goal II:

Assist in the expansion and improvement of the state's economy through the development of high value jobs and the diversification of the economic base.

- Increase responsiveness to workforce development needs by expanding and developing programs in high demand fields in the state, as measured by
 - Employer satisfaction with graduates (4)
 - Degrees and certificates awarded in high-demand occupational fields (2)
 - Job placement rates (2)
 - Growth in enrollment, for certificates and degrees, in 2-year programs (2).
- Establish collaborative programs among institutions, the private sector, and the state to expand research, technology transfer, the commercialization of new technologies, and the development of our entrepreneurs, as measured by
 - Research & development receipts and expenditures (2)
 - Technology licenses with Montana businesses (1).

Shared Goal III:

Improve institutional and system efficiency and effectiveness.

Improve the accuracy, consistency and accessibility of system data, including the continued development of a comprehensive data warehouse (1, 3).

Deliver efficient and coordinated services, as measured by

- Improve articulation and transferability among all 2-year and 4- year institutions, including community colleges and tribal colleges (2).
- Expenditures per student relative to peer institutions and historical levels
- Percentage of expenditures in the following areas (2):
 - Instruction
 - Research
 - Public Service
 - Academic Support
 - Student Services
 - Institutional Support
 - Plant O&M
 - Scholarship and Fellowships
 - Other

Reconstruct the budget allocation model consistent with state and system policy goals and objectives (1).

AGREEMENT

WHEREAS, Article VIII, section 12, of the Montana Constitution vests in the Legislature the responsibility to ensure strict accountability of all revenue received and spent by the state, counties, cities, and towns and all other local governmental entities; and

WHEREAS, Article X, section 9, of the Montana Constitution vests in the Board of Regents of Higher Education the full power, responsibility, and authority to supervise, coordinate, manage, and control the Montana University System and to supervise and coordinate other public institutions assigned to it by law; and

WHEREAS, the Joint Subcommittee on Postsecondary Education Policy and Budget (PEPB), comprised of members representing the Montana Legislature, the Montana Board of Regents, and the Executive Branch, has identified statewide public postsecondary education policy goals and accountability measures with the input and feedback of the Montana University System;

This AGREEMENT, between the Joint Subcommittee on Postsecondary Education Policy and Budget and the Montana University System, identifies the statewide public postsecondary education policy goals and related accountability measures (see pages 1-3 above) that will be used as a policy goal setting and assessment tool for policymakers, the university system, and the public in evaluating the achievement of the policy goals; and that will be used as a guide to drive decision packages and funding mechanisms for the state funding that is appropriated to the Montana University System by the Montana State Legislature.

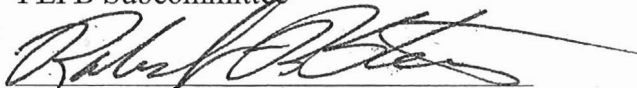
The parties further agree to:

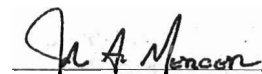
1. The Montana University System shall prepare a Shared Policy Goals and Accountability Measures Report presenting appropriate and current data for these goals and accountability measure in an easy-to-read format.
2. The Shared Policy Goals and Accountability Measures Report shall be presented to the House and Senate Education Committees and the Joint Appropriations Education Subcommittee by the 10th legislative day of the 60th Legislature (2007 legislative session).
3. The Shared Policy Goals and Accountability Measures Report shall be posted to the Board of Regents website and the Joint Subcommittee on Postsecondary Education Policy and Budget website by January 1 each year that the update is due.

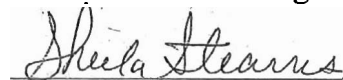
This agreement expires January 1, 2009.

Dated this 22 day of 200.


Rep. Kathleen Galvin-Halcro, Chairman
PEPB Subcommittee


Senator Robert Story, Vice Chairman
PEPB Subcommittee


John Mercer, Chairman
Montana Board of Regents


Sheila Stearns, Commissioner
Commissioner of Higher Education



Postsecondary Education Budget and Policy Committee

The Mechanics of House Bill 2 (HB2)

Staff Presentation

Thursday, December 1, 2005

Presentation Outcome Goal: That PEPB subcommittee members understand how to achieve and implement potential legislative options related to Project #1 (Budgeting through the use of Policy Goals/Accountability Measures as budget drivers) and Project #2 (Funding Formula Changes).

Why Spend Time On This: To clarify the technical mechanisms that are used in House Bill 2 (HB2) to provide state funding to the MUS so that work plan projects and potential PEPB legislative options are formulated properly and may be considered for implementation in the HB2 budget for the 2009 biennium.

Brief Review:

The state budget and HB2 for the Montana University System (MUS) is organized by Program:

Commissioner of Higher Education Functions

Program 1 = Administration
Program 2 = Student Assistance (Financial Aid)
Program 3 = Improving Teacher Quality
Program 6 = Talent Search (Student Support Programs)
Program 8 = Workforce Development
Program 12 = Guaranteed Student Loan
Program 13 = Board of Regents Administration

- Base Year + Present Law + New Proposals = BUDGET

Community Colleges

Program 4 = Community College Assistance

- FTE Students x Cost of Education x State % Share (policy decision made each biennium) = BUDGET

Medical and Workers Comp Insurance

Program 5 & 7 ... these are proprietary funds (rates are approved based on fee for service basis)

University Educational Units

Program 9 = Distribution to University Campuses and Research/Public Service Agencies

- **Research/Public Service Agencies** (Extension, Ag. Experiment, Bureau of Mines, Forestry, Fire School):
Base Year + Present Law + New Proposals = BUDGET
- **University Education Units**
- Base Year + (Present Law x State % Share¹) + (Marginal Cost Per Student x FTE Growth) + New Proposals = BUDGET

Tribal Colleges

Program 11 = Tribal College Assistance

- Actual Budget Formula → Typically no specific formula is applied...rather an appropriation level is determined based on budget affordability that remains below the statutory ceiling...while historical guidance is considered based upon the average FTE enrollment of 311 per year

State Also Funds the State Pay Plan → House Bill 447 (in the 2007 biennium budget)

For the Montana University System, the state pay plan funds only the state % share of the cost of the pay plan at the university units (recall that the state % share in the 2007 biennium is 39%), which leaves the remaining 61% of the costs of the state pay plan to be paid by other sources, primarily tuition.

Therefore...to effect change in HB2 funding for the MUS related to either Project #1 or Project #2 PEPB must:

1. Change the method/calculation to determine the Base year funding level
2. Change the calculation method for the State % Share that determines many funding levels, including the Present Law Adjustments and the Pay Plan
3. Change the method of calculating and implementing Present Law Adjustments
4. Implement New Proposals

Let's consider these in reverse order, which also leads from simplest to most complex:

- **New Proposals:**

These are Decision Packages² (DP's) that provide new funding, above the Base and Present Law Adjustments, to support either existing program goals/objectives at a higher service level with new funding or to support new programs to achieve new goals/objectives. New Proposal DP's may simply state an amount given for a general purpose, or the DP can list specific goals/objectives to be achieved with the funding (see examples below). These DP's may be restricted to spending only for that specific purpose, they may be approved as One-time-only (OTO) so that the funds do not "roll into the base" for the next biennium, etc. Thus, to affect change in HB2 funding for New Proposals is a function of how the DP's are written (e.g. setting measurable goals, incentive funding, restricting the funding, OTO's, etc.). For example:

- An actual from HB2... DP 78 - Equipment/Program Development - 2 Yr Programs-OTO - The legislature approved a restricted, biennial, one-time-only appropriation of \$4.46 million general fund in the 2007 biennium to fund the purchase and update of equipment and program development for two-year degree programs that is to be distributed in two blocks as follows: (1) \$1.4 million must be allocated equally (\$200,000 per unit) to the seven university units' 2-year degree programs to be used for either program development or equipment acquisition; and (2) \$3.06 million must be distributed entirely by a competitive grant process administered by the Office of the Commissioner of Higher Education. These equipment grants will be available to both the seven university units' 2-year degree programs and the three community colleges (Dawson, Miles, and Flathead Valley). The equipment portion of this appropriation must be matched from non-state funds identified by the Board of Regents.
- An actual from HB2... DP 1011 - Distance Learning Initiative - OTO - The legislature approved \$300,000 general fund in the 2007 biennium to support the development and implementation of a statewide distance learning plan across the university system and partnering with education providers at all levels. This was approved as a biennial, one-time-only appropriation.
- A potential from policy goals... DP 4 – Promote Access and Affordability for Montana Students as Compared to Median Family Income – The legislature approves an annual appropriation of \$ ____ to each of the university system educational units for each year of the biennium that each unit is able to keep tuition rates at or below a level that represents ____ percent of the median

family income of Montana residents, up to a maximum appropriation of \$ _____. This will be a one-time-only (OTO) appropriation.

- ~~An actual from HB2...~~ DP 3 – Increase Responsiveness to Workforce Development Needs in High-Demand Occupations – The legislature approves an annual appropriation of \$ ____ to each of the university system educational units for each year of the biennium that each unit is able to increase by ____ percent or by ____ number the level of degrees or certificates awarded in high-demand occupational fields.

• **Present Law Adjustments:**

These are DP's that provide funding, above the Base, in order to maintain "current law" programs at their required level of service (not new services). Typically present law adjustment DP's reflect inflationary cost increases or student enrollment increases, where additional funding is required to maintain the current level of service. Once again, Present Law DP's may simply state an amount given for a general purpose, or the DP can list specific goals/objectives to be achieved with the funding. These DP's may be restricted to spending only for that specific purpose, they may be approved as One-time-only (OTO) so that the funds do not "roll into the base" for the next biennium, etc. Thus, to affect change in HB2 funding for Present Law Adjustments is a function of how the DP's are written, as well as how the adjustment calculations are made (e.g. which inflation index is used, the State % Share level, etc.).

- ~~An actual from HB2...~~ DP 21 - Additional Federal Funds for Student Assistance - The legislature added \$73,574 additional federal authority in the 2007 biennium for anticipated increases in federal funds for student grants. These funds will be used as the federal match portion in the state matched Baker Grant program.
- ~~An actual from HB2...~~ DP 43 - Increased IT License and Maintenance - The legislature approved \$298,000 general fund in the 2007 biennium to fund the state share calculation of increased information technology licenses and maintenance costs at MSU-Bozeman, UM-Missoula, MSU-Billings, Montana Tech, UM-Western, and the Helena College of Technology.
- ~~A potential from policy goals...~~ DP 2 – Make Higher Education More Affordable by Offering Need-based Student Financial Aid to More Students – The legislature increases the ____ student assistance program by \$ ____ to increase the percentage of students in the MUS who receive need-based financial aid by at least ____%. This appropriation is restricted to the ____ student assistance program and will be an OTO appropriation.
- ~~A potential with new state % formula...~~ DP 3 – Present Law Adjustment for Operations and Maintenance – The legislature approved \$ ____ general fund to support inflationary increased cost adjustments for building operations and maintenance at the university educational units at the state percentage share of ____% (which represents a formula based upon ____).

• **State % Share:**

Currently this percentage represents the ratio between the total cost of education for Montana resident students and the portion of those costs paid by state funds (as opposed to tuition). This calculation model is NOT driven by statute but is a budget policy decision, so that to effect change, the legislature has the policy authority to change the calculation model without a bill draft and statute change.

- *As a ratio between Montana resident students vs. Non-resident students...* this calculation model was used for some present law adjustments in the 2007 biennium budget. The result is a state % share at the 80% level...which is the current percentage of resident students attending the university educational units.

- *As a pure policy decision by the legislature...* this calculation model is used by the legislature (since 1982) to determine the state funding level for the community college assistance program. The legislature states, in HB2, the percentage of the cost of education that state policy goals determine as the level to support Montana resident students. Currently the legislature has set that level at 53% for the community colleges.

- **Base Funding Level:**

Currently, the base funding is determined by taking the actual expenditures from the last completed fiscal year, removing OTO's and budget amendments, and that calculation sets the "base funding level" upon which the budget is built. Barring any extraordinary cost increases during a base year or any economic crisis affecting state revenue, the executive and legislature typically accept base year funding levels as determined from past expenditures.

In the university educational units budget, that base combines expenditures for fixed costs (such as utilities and other operations and maintenance costs that are not truly correlated to student enrollment) together with expenditures for variable costs (such as consumable supplies and adjunct faculty costs that fluctuate as a function of student enrollment). Under the current formula, there is no calculation that attempts to distinguish fixed vs. variable costs so that base year expenditures in total become the "base" for the next biennium budget.

At that point, the Present Law Adjustments and the New Proposals, in the form of DP's, build up from the base to become the budget. This model is essentially an "Incremental Budget Model"... change to the past expenditure level, the Base, is the focus of the budget process through specific DP's that essentially adjust the Base for inflation and to fund new proposals.

Other Base budget calculation models could include the following:

- Zero-based budgeting...starting with a zero budget each fiscal year and require that all expenditures be justified in budget detail
- Three-factor funding formula...used for the community colleges...could be used to establish Base funding level for university units then add new proposal DP's. The three factors are:
 - FTE Students x Cost of Education x State % Share (policy decision made each biennium)
 - Then legislature sets a specific % share of the base that it will fund...may want to fund differently for 4-year vs. 2-year, for fixed vs. variable, etc.
- Fixed vs. Variable Cost model...base funding level could be determined using two categories of expenditures, fixed and variable, and then use separate calculations to make incremental adjustments to each type of expenditure. This base calculation formula could more accurately portray the costs.

Effecting change to base funding becomes much more complex than any of the above, both in term of complexity of details and complexity of making calculations.

Conclusion:

Therefore, in the event that PEPB decides to move forward to implement budget initiatives in HB2 that come out of workplan projects #1 or #2 the mechanisms to move these initiatives forward include:

1. **New Proposal Decision Packages (DP's)**...to create new programs and add new funding...and these may be written to include goal setting and measurable objectives that are intended to be achieved. In addition, the funding may be restricted for spending only on these specific programs, and made one-time-only so that continued funding would be subject to subsequent evaluation of progress/success against the measurable objectives that are written. Incentive funding could also be written into new proposal DP's.
2. **Present Law Adjustment Decision Packages (DP's)**...to fund existing services at levels required under present law...just as with New Proposals, the present law adjustment DP's could be written to include policy goals or they could be calculated with different adjustment formula (perhaps a specific inflation index specified). In addition, change can be affected to present law funding by changing the calculation of the state % share, as that calculation is a multiplier that determines the funding level of present law adjustments.
3. **State percentage (%) share**...the state share of funding to pay a proportion of the costs of education at the university units...this is used to determine funding for Present Law Adjustment DP's and the State Pay Plan...this percentage may be calculated in various ways...or it may be a purely public policy decision that is made by the legislature based upon policy goals and available state revenue.
4. **Base funding level**...currently this is the ongoing expenditures from the most recently completed fiscal year...affecting change to the base is more complex but it could be done by adopting alternate formula models.

This presentation was not intended to be advocating for any of the models discussed but merely to provide an understanding of the budget mechanisms that are used in HB2 so that PEPB, and by extension the legislature, will have to tools needed to implement any budget options that come out of these workplan projects.

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¹ Recall that the "state % share" in the budget for the University Educational Units is **NOT** driven by a stated legislative policy decision, as it is in the Community College budget. Rather, "State % Share" is the ratio of state funds as part of the Current Unrestricted Operating Fund (that fund which pays the basic costs of educating students) ... thus, going into the last budget, the "State % Share" was 43% ... meaning that 43% of the funding to pay for the basic costs of educating students was state funding...so that the Present Law Adjustments, the updating of the budget for cost changes, would be funded by the state at 43%. There are some mathematical anomalies to this formula, however, so that it is on a mathematical trend downward, independent of public policy decisions...for example, coming out of the last state budget adopted in the 2005 legislative session, the state % share is now about 39%...which is 4% less than coming into the session...

² Decision Packages (DP's) are specific, discreet funding amounts to be appropriated by fiscal year in the HB2 biennium budget to provide funds a specific program, purpose, etc. To be approved by the legislature, each DP must be subject to a vote, as DP's are stated separately from the budget base.

Montana University System Initiatives

Priority	Initiative	Amount	Brief Description of Initiative
1	Improve Transferability and Student Data	\$1,900,000	Funds needed data systems, faculty program council expenses, and P-20 work (\$1.3 million OTO); and sustainability of initiative (\$600,000).
2	Expand Indian Education for All	\$500,000	Funds programs needed to implement IEFA at postsecondary institutions.
3	Improve Affordability	\$3,900,000	Includes MPACT scholarship program (\$2.5 million) and 2-year program tuition buy-down (\$1.4 million).
4	Coordinate and Expand Distance Learning	\$600,000	Continue implementation of distance learning coordination and program expansion, including creation of "gateway" for MUS distance programs.
5	Healthcare Worker Education	\$4,900,000	Includes developing healthcare worker strategic plan, creation of data and program advisory groups, expansion of WWAMI medical school (\$1.9 million) and new allied health programs, principally in 2-year colleges, to address critical shortage areas (\$3 million).
6	Create Montana Energy Center	\$2,000,000	Create a Montana Energy Center to coordinate and promote energy development (including research) in Montana.
Total		\$13,800,000	

Source: Office of the Commissioner of Higher Education



Postsecondary Education Budget and Policy Subcommittee

Alternative State Funding Models for Higher Education

Staff Presentation

Thursday, February 23, 2006

Presentation Outcome Goal:

As part of PEPB Project #2, subcommittee members are interested in **reviewing** the current funding formulas that drive state funding levels for higher education (specifically the university educational units) and then **looking at alternative models** for state funding in order to determine if the PEPB would like to consider other funding models or mechanisms for higher education funding. In the prior staff report "The Mechanics of House Bill 2 (HB2)" all of the current funding formulas in the Montana budget are presented. It is the intention of **this report** to review other models for PEPB discussion and consideration.

If the PEPB determines that any of the model options presented in this report have the potential to present preferred outcomes compared to the existing model, PEPB may want to instruct staff to conduct additional research and report back with specific action options.

If PEPB is interested in making budget model recommendations to influence the 2009 biennium budget, that recommendation would be forwarded to the Governor's Budget Office for consideration as the executive initiates the budget process and prepares the Executive Budget that is then submitted to the legislature.

Why Spend Time On This Issue Report:

To look at funding models in other states to see if there is a "best-practices" model or other funding mechanism that may demonstrate advantages or other public policy distinctions to the Montana funding model. The goal of this review is to either identify a model for consideration or stimulate thinking that leads PEPB to devise other models or mechanisms.

Brief Review:

In Montana, the state budget funds the university educational units using the following model:

University Educational Units

Base Year + (Present Law x State % Share¹) + (Marginal Cost Per Student x FTE Growth) +
New Proposals = BUDGET

State Also Funds the State Pay Plan →

For the Montana University System, the state pay plan funds just the state percent share of the cost of the pay plan at the university units (recall that the state percent share in the 2007 biennium is approximately 39 percent), which leaves the remaining 61 percent of the costs of the state pay plan to be funded by other sources, primarily tuition.

Funding Models from Other States:

Attached to this report is an inventory of data and narratives received from other states from a national request by the National Conference of State Legislatures and by the Legislative Fiscal Division (LFD). Using this inventory as a starting point, the following are some of the responses received regarding funding models for higher education from other states.

Arizona - No data received on their specific funding model, but the legislature does build performance measures into the general appropriations act for each campus in order to make clear what they seek to "purchase" with state funds. This process may lead to incentive funding in the future, which would provide additional state funds if targets are met/exceeded.

Arkansas – No data received on their specific funding model, but the legislature has created a \$1 million incentive funding pool and provides additional funds when specific accountability measures are met.

Idaho – Same model as Montana: Higher education budget = Base + Adjustments + New Proposals
Enrollment change funding is determined by looking at 3-year rolling averages of student enrollment levels (Montana enrollment funding uses projections for each year).

Kansas – No data received on their specific funding model, but starting with Fiscal Year 2006 any new state funding shall be contingent upon that campus achieving the goals set in an accountability measures agreement with the state.

Michigan – Allocates funding with a formula based on three components:

- Enrollment-based component (37.5% of total funding) ... as universities receive a base funding amount per FTE student, with resident students funded at a higher level than non-resident students
- Degree-based component (37.5% of total funding) ... as universities receive a base funding amount for the different types of degrees conferred, with higher cost degrees funded at a higher level (e.g. science and engineering)
- Research-based component (25% of total funding) ... as universities receive state matching funds for federal research grants in science and engineering

Nebraska – Same as Montana: University Budget = Prior Year Base + Adjustments + New Initiatives

New Jersey - No data received on their specific funding model, but each campus can earn up to 1 percent additional state funding if they meet accountability measures for graduation rates, transfer and articulation, efficiency and effectiveness, and diversified revenues.

North Carolina – Same model as Montana: University Budget = Base Year + Inflation Adjustments ... in addition, enrollment change funding uses a complex model that looks at the cost of each program, the instructional level, and student enrollment projections.

North Dakota – Same as Montana: University Budget = Base Year + Inflation Adjustments ... but also ties funding level to the state's sustainable revenue growth so that if the state economy improves and state revenue increases, the university system gets a fixed percentage increase correlating to that growth.

South Carolina - No data received on their specific funding model, but approximately 3 percent of state funding for the campuses is tied to their performance in 9 "critical success areas" as measured by 37

performance accountability measures. State expects to increase the amount of funds that are appropriated in this manner.

Washington – Same as Montana: University Budget = Base + Increment Adjustments + Initiatives

Legislative Options for Consideration:

Should the PEPB decide to consider alternative funding mechanisms in order to influence the state funding level for the Montana University System, the following are options to consider:

*[Sidebar – in the one area where state government has codified a budgeting formula for the university system, in the community college program, the legislature identifies (in the 1981 funding study that led to the formula) that an underlying policy goal of that formula is to be **Transparency**; that the formula be clear, concise and easy to understand. In the options below, that legislative policy goal has been considered by LFD staff]*

COST OF EDUCATION MODELS

Three-factor funding formula model to establish the base-year budget (currently used by the community college funding program):

Stated mathematically, this funding formula looks like the following:

- $\text{Student Enrollment} \times \text{Cost of Education} \times \text{State Percent Share} = \text{General Fund Budget Base}$
(e.g. 100 Students x \$100 Cost Per Student x 53% State Share = \$5,300 General Fund Base)

Requires that the executive, legislature and the Board of Regents can reach agreement on a method to calculate the cost of education that all will trust and accept.

In this model, base-year funding is established as a direct function of the policy decision on what the **State Percent Share** level will be. That policy decision would be made in the original executive budget and then reviewed by the legislature in the HB2 process. Thus, each budget would determine what percent of the costs of education that state government would be able to fund; based upon public policy and available revenue.

Recall that in the current funding model, the state percent share is based on a mathematical formula that inherently decreases if universities raise tuition or spend more than state expenditure projections. So the primary change in this model is that the state percent share becomes a conscious policy decision rather than a pre-determined mathematical outcome. This would make the budget much more transparent and make it more subject to clear public policy goals rather than a function of confusing mathematical formulas.

Fixed and variable costs of education model (variation of the three-factor funding formula above):

Stated mathematically, this formula would look like the following:

- $\frac{[(\text{Student Enrollment} \times \text{Variable Cost of Education}) + \text{Fixed Cost of Education}]}{\text{State Percent Share}} = \text{General Fund Budget Base}$
e.g. $\frac{[(100 \text{ Students} \times \$40 \text{ Variable Cost Per Student}) + \$6,000 \text{ Fixed Cost}]}{53\% \text{ State Share}} = \$5,300 \text{ General Fund Base}$

This model is essentially the same as above, in terms of the exercise of public policy and the need for an acceptable cost of education factor.

But this model accounts for the fixed cost base that university units experience...as not all costs are driven by the number of students who enroll.

This model would require that the executive, legislature and the Board of Regents could reach agreement on a method to calculate the ratio of fixed to variable costs in each campus budget so that all will trust and accept that calculation. Of course, once again, the ultimate funding level is determined by the public policy decision on the State Percent Share level.

BASE PLUS ADJUSTMENT WITH STATE PERCENT SHARE POLICY DECISION

Current model, but for the state percent share is purely a legislative policy decision:

- $\text{Base Year} + (\text{Present Law} \times \text{State \% Share}) + (\text{Marginal Cost Per Student} \times \text{FTE Growth}) + \text{New Proposals} = \text{BUDGET}$

This model only changes the State Percent Share factor by making it purely a public policy decision, rather than a mathematical formula. It would operate such that the executive budget would recommend a percent level based upon policy goals and revenue affordability, and the legislature would consider that and make a decision that is stated in HB2.

This would make the budget much more transparent and make it more subject to clear public policy goals rather than a function of confusing mathematical formulas.

Current model but for the state funding level is a function of targets set as a policy goal of the "proper" state funding/tuition mix (that target mix could be based upon a peer institution average or norm):

- $[\text{Base Year} + \text{Present Law} + (\text{Marginal Cost Per Student} \times \text{FTE Growth})] \times \text{State \% Share} + \text{New Proposals} = \text{BUDGET}$

Under this model the state budget would identify the total cost of the university system budget and then determine the State % Share factor by setting a target, based upon a public policy decision, for the desired ratio between state funding/student tuition, so that the level of the state percent share decision would be a policy decision driven by a target ratio of state/tuition funding. Such a ratio could be determined and based upon peer institution norms.

This model would require that the executive, legislature and the Board of Regents could agree on appropriate peer institutions.

The targets would not require absolute agreement but could be target goals that each branch (executive and legislature) defines somewhat differently.

Once again, this model would be transparent and would shift the State Percent Share factor from a mathematical outcome to a public policy decision, but in this model that public policy decision is couched within a specific target range, that being a ratio from peer institution norms.

FUNDING THE PAY PLAN FOR THE UNIVERSITY SYSTEM

As stated above, the current practice for pay plan funding for the university system is that the pay plan bill calculates the total impact of salary/benefit changes on the university units budget, and then funds the pay plan at the State Percent Share level. Thus, in the 2007 biennium budget the university units received approximately 39 percent of the total funding they would need to meet the state pay plan.

An alternate model could be to fund the pay plan using a different calculation for the State % Share:

- ◆ The State Percent Share calculation for the pay plan could be purely a public policy decision so that the statute states the specific percentage of the total funding that the state would provide, based upon available revenue and policy goals.
- ◆ The State Percent Share calculation for the pay plan could be based upon a desired ratio between state funding/student tuition, with that target ratio derived from a comparison with peer institutions to identify a norm level of state/tuition funding levels.

INCENTIVE FUNDING POOL

Current model but tie additional funding level increases to successfully achieving policy goals and accountability measures

- State the accountability measures in HB2 for the first year of the biennium that trigger incentive funding
- If targets are met by the end the first year then incentive funds are available in the second year of the biennium
- The incentive funds could be appropriated as unrestricted funding or targeted/restricted for certain purposes

CONCLUSION

If the legislature is interested in affecting the state budget for the Montana University System at the base rather than just in the area of new proposals, legislators may want to consider selecting one or more of these model options for further investigation, including potential scenarios and comparatives to prior budgets. Based upon that additional investigation and modeling, subsequent PEPB action options may include the following:

1. Discuss with the Office of Budget and Program Planning a package of changes to the higher education funding model for the 2009 biennium budget, perhaps advocating for a specific model
2. Recommend pilot implementation of an alternative funding model(s) to the Office of Budget and Program Planning for a specific component of the higher education budget
3. Request a bill draft for a comprehensive funding study during the 2007-2008 interim

A decision about these action options does not need to be made at the February meeting, but they are listed here to provide “sideboards” for the process going forward in the June 2006 PEPB meeting.

FEBRUARY MEETING DECISION POINTS

The following are decision options, based upon the alternative funding model options, for PEPB consideration at the February 2006 meeting:

1. Do nothing at this time on alternative funding models for the Montana University System
2. Select one or more alternative models for further investigation and development of illustrations, to be presented to PEPB at the June meeting
3. Invite the Office of Budget and Program Planning to the June meeting and request a briefing on the status of the postsecondary education budget for the 2009 biennium, with particular attention to the funding models for the university units

¹ Recall that the “state % share” in the budget for the University Educational Units is **NOT** driven by a stated legislative policy decision, as it is in the Community College budget. Rather, “State % Share” is the ratio of state funds as part of the

Current Unrestricted Operating Fund (the fund which pays the basic costs of educating students). Thus, going into the last budget, the "State % Share" was 43% (meaning that 43% of the funding for the basic costs of educating students was state funding) and so the Present Law Adjustments, updating the budget for cost changes, would be funded by the state at 43%. There are some mathematical anomalies to this formula, however, so that it is on a mathematical trend downward, independent of public policy decisions. For example, coming out of the state budget adopted in the 2005 legislative session, the State % Share is now about 39%, which is 4% less than going into the session.

*Second Budget
to
Honors
Scholar*

Schedule A
Governor's Postsecondary Scholarship
Year 1 Allocation Summary
FY2006

Institution	Merit High School Scholarships \$	Merit At-Large Students Scholarships \$	Need General Scholarship Scholarships \$	Need Health Sciences Scholarships \$	Need Technology Scholarships \$	Total Scholarships \$
University of Montana	\$1,000 per award 42 \$ 42,000	\$2,000 per award 8 \$ 16,000	-	-	-	50 \$ 58,000
Montana State University Bozeman	73 \$ 73,000	8 \$ 16,000	-	-	-	81 \$ 89,000
MSU - Billings	13 \$ 13,000	3 \$ 6,000	-	-	-	16 \$ 19,000
MT Tech of UM - Butte	12 \$ 12,000	2 \$ 4,000	-	-	-	14 \$ 16,000
MSU - Northern	4 \$ 4,000	1 \$ 2,000	-	-	-	5 \$ 6,000
WMC of UM	3 \$ 3,000	1 \$ 2,000	-	-	-	4 \$ 5,000
Salish Kootenai College	1 \$ 1,000	1 \$ 2,000	-	-	-	2 \$ 3,000
Total 4-year	148 \$ 148,000	24 \$ 48,000	-	-	-	172 \$ 196,000
Flathead Valley Community College	\$1,000 per award 2 \$ 2,000	\$1,000 per award 8 \$ 8,000	\$1,000 per award 18 \$ 18,000	\$1,000 per award 11 \$ 11,000	\$1,000 per award 24 \$ 24,000	63 \$ 63,000
College of Technology - Great Falls	1 \$ 1,000	5 \$ 5,000	13 \$ 13,000	7 \$ 7,000	16 \$ 16,000	42 \$ 42,000
College of Technology - Missoula	5 \$ 5,000	4 \$ 4,000	9 \$ 9,000	5 \$ 5,000	12 \$ 12,000	35 \$ 35,000
College of Technology - Helena	1 \$ 1,000	3 \$ 3,000	8 \$ 8,000	5 \$ 5,000	10 \$ 10,000	27 \$ 27,000
College of Technology - Billings	3 \$ 3,000	3 \$ 3,000	8 \$ 8,000	4 \$ 4,000	10 \$ 10,000	28 \$ 28,000
Miles Community College	5 \$ 5,000	2 \$ 2,000	6 \$ 6,000	3 \$ 3,000	7 \$ 7,000	23 \$ 23,000
Blackfeet Comm College	-	2 \$ 2,000	4 \$ 4,000	3 \$ 3,000	6 \$ 6,000	15 \$ 15,000
Fort Peck Community College	1 \$ 1,000	2 \$ 2,000	4 \$ 4,000	3 \$ 3,000	6 \$ 6,000	16 \$ 16,000
Dawson Community College	1 \$ 1,000	2 \$ 2,000	4 \$ 4,000	2 \$ 2,000	5 \$ 5,000	14 \$ 14,000
Stone Child College*	-	1 \$ 1,000	3 \$ 3,000	2 \$ 2,000	4 \$ 4,000	10 \$ 10,000
College of Technology - Butte	-	1 \$ 1,000	3 \$ 3,000	2 \$ 2,000	3 \$ 3,000	9 \$ 9,000
Little Big Horn College	1 \$ 1,000	1 \$ 1,000	2 \$ 2,000	1 \$ 1,000	3 \$ 3,000	8 \$ 8,000
Fort Belknap College	1 \$ 1,000	1 \$ 1,000	2 \$ 2,000	1 \$ 1,000	3 \$ 3,000	8 \$ 8,000
Dull Knife Memorial College	1 \$ 1,000	1 \$ 1,000	1 \$ 1,000	1 \$ 1,000	1 \$ 1,000	5 \$ 5,000
Total 2-year	22 \$ 22,000	36 \$ 36,000	85 \$ 85,000	50 \$ 50,000	110 \$ 110,000	303 \$ 303,000
Total Available	180	60	85	50	110	485
Left to Allocate	10	0	0	0	0	10
Schools not participating	-10	0	0	0	0	-10

Document Source:

Office of Commissioner of Higher Education
MT Guaranteed Student Loan Program
(Dec 2005)